IN THE

Supreme Court of the United States

October Term, 1974

No. 74-157

UNITED HOUSING FOUNDATION, INC. *et al.*,
Petitioners,

v.

MILTON FORMAN and ELLEN FORMAN, *et al.*,
Respondents,

and

THE STATE OF NEW YORK and the
NEW YORK STATE HOUSING FINANCE AGENCY,
Additional Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

PETITIONERS' REPLY MEMORANDUM

SIMON H. RIFKIND
345 Park Avenue
New York, New York 10022
Attorney for Petitioners

MARTIN LONDON
GEORGE P. FELLEMAN
ALAN G. BLUMBERG
Of Counsel

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PETITIONERS' REPLY MEMORANDUM

Petitioners submit this memorandum in reply to new matters raised by respondents in their brief in opposition to the Petition for Certiorari.

1. The respondents incorrectly argue that the judgment of the Court of Appeals is not ripe for review because it is interlocutory (R 6-7).* However, this Court has frequently reviewed interlocutory judgments involving issues " 'fun-

* References to the respondents' brief appear as: (R 11); and to the printed appendices filed with this Court as: (A 16).

damental to the further conduct of the case,'" particularly judgments, such as this, involving important questions of federal court jurisdiction.* *Larson* v. *Domestic & Foreign Commerce Corp.*, 337 U.S. 682, 685 n. 3 (1949); *Land* v. *Dollar*, 330 U.S. 731, 734 n. 2 (1947); R. Stern & E. Gressman, *Supreme Court Practice* §4.19 at 180-81 (4th ed. 1969). And see *United Steelworkers of America* v. *R. H. Bouligny, Inc.*, 382 U.S. 145, 146-47 (1965), cited in the Petition. Indeed, notwithstanding the interlocutory status of this case, the Court of Appeals for the Second Circuit recognized the possibility of Supreme Court review of this jurisdictional question and stayed the issuance of its mandate pending this Court's disposition of the Petition for Certiorari.

2. As described in the Petition, the decision below substantially undermines the long-established definition of an investment contract under the federal securities laws. Attempting to explain that decision, respondents argue that the Court of Appeals held that profit "inducements, . . . offered to purchasers . . ." were "substantial and real" (R 11). That is a significant distortion of the findings of the Court of Appeals and underscores the confusion the decision has generated and the need for review by this Court.

The Court of Appeals, like the District Court, did not find that petitioners made any promises or inducements of profits; rather, it found that elements of "profit"—as it incorrectly construed that term—might be available to cooperative members. Thus it found not the promise of profits, but that cooperative members may in fact share in

* None of the cases cited by respondents involves the review of a jurisdictional question.

rental income from the cooperative's commercial facilities, may take advantage of certain tax benefits, and probably pay lower-than-market housing costs (A 16-17).* But those benefits (which were not used to induce the purchase of the cooperative memberships) are remote from the profit inducement and economic lure which this Court has held to be indispensable elements of an investment contract.**

3. SEC Rule 235, 17 C.F.R. §230.235, relied upon by respondents, does not "implicitly recognize . . . that the stock of a cooperative housing corporation [is] a security" (R 12). Rather, as noted by Professor Loss, "it would be too facile to argue that [Rule 235] proves conclusively that [cooperative] shares are securities under either the 1933 Act or 1934 Act." 1 Loss, SECURITIES REGULATION 493-94 (1961). The District Court properly concluded that Securities Act Release No. 5347, not Rule 235, represents the more current and considered view of the SEC.†

And, contrary to respondents' argument, Securities Act Release No. 5347 expressly refers to "condominium and cooperative unit[s]," (D 11) and not just to condominiums. And even if respondents were correct that Securities Act Release No. 5347 applies only to condominiums, a funda-

* Further, although respondents asserted in their Statement of the Case that petitioners set forth these inducements in their Information Bulletins (R 5-6), the very pages of the Bulletin cited by respondents do not promise any commercial rental income, specifically warn that there is no promise of tax deductions, and refer not to below-market housing prices but to "decent housing at a reasonable price."

** See discussion and cases cited in the Petition, pp. 20-23.

†". . . [T]he S. E. C. itself has refined its thinking and is now seeking to narrow its interpretation of the scope of the securities acts to those housing enterprises where all three-prongs of the *Howey* [investment contract] test are present" (B 29). Moreover, the courts are not bound by an administrative determination, such as Rule 235, which has never been tested in court. *SEC* v. *Sterling Precision Corp.*, 393 F.2d 214, 220 (2d Cir. 1968). See also comment of the District Court at B 28-29.

mental conflict remains, since the sweeping decision below defines the "profit" prong of the investment contract test in a manner expressly rejected by the Release. There is no rational basis for holding that "profit" necessary for an investment contract has one definition when applied to a cooperative and an inconsistent definition when applied to a condominium. The considerable confusion generated by this conflict, as reflected in the recent professional and industry literature, is all the more reason for this Court to review the judgment of the Court of Appeals.

4. Respondents have grossly distorted the facts and posture of this case in arguing that petitioners seek to use their "professed 'eleemosynary'" status to excuse fraudulent conduct (R 11-12).*

That is an irresponsible argument. Respondents deal violently with the record and petitioners' argument by suggesting that they will be deprived of a forum to air their alleged claims if this Court agrees that the federal courts lack jurisdiction. The issue in this case has always been whether respondents' claims should be litigated in the state, rather than federal, courts.** That issue involves

* Contrary to respondents' baseless claim, petitioner United Housing Foundation is, as both the District and Circuit Courts found, a nonprofit corporation.

** It should be noted that this case could be litigated in the New York State courts without the difficult and complex Eleventh Amendment problem created by respondents' joinder as defendants of the State of New York and the New York State Housing Finance Agency. In this regard, the petition of the State of New York and the New York State Housing Finance Agency for rehearing in the Court below was denied on September 12, 1974, and we are advised that they plan to petition this Court for a writ of certiorari. Because of the significant constitutional questions present in this case by reason of the State's involvement as a defendant, this Court might wish to defer consideration of this petition until the State has filed and all parties are before the Court.

an important and unsettled question of federal court jurisdiction which should be decided by this Court.

Conclusion

The substantial and important jurisdictional question raised by this case cannot be obscured by respondents' description of the issue as insignificant and well settled.

Did Congress, in enacting the Securities Act of 1933 and the Securities and Exchange Act of 1934, intend to sweep within their ambits purchases and sales of state-subsidized and regulated private residences built by nonprofit agencies, pursuant to state housing programs? That issue is of signal importance to state and municipal governments, the private housing industry and the administration of the federal securities laws. It deserves resolution by this Court.

Dated: New York, New York
September 26, 1974.

Respectfully submitted,

SIMON H. RIFKIND
345 Park Avenue
New York, New York 10022
Attorney for Petitioners

MARTIN LONDON
GEORGE P. FELLEMAN
ALAN G. BLUMBERG
Of Counsel